No. 09-981

Supreme Court, U.S.
FILED
MAY 3 - 2010
OFFICE OF THE CLERK

In The
Supreme Court of the United States

JOHNSON CONTROLS, INC.; SECURITY GROUP, INC. AND SUBSIDIARIES, INCLUDING SARGENT & GREENLEAF, INC.; WILLIS NORTH AMERICA, INC. AND AFFILIATES; BUNZL USA, INC. AND SUBSIDIARIES INCLUDING MAK-PAK, INC.; TREDEGAR CORPORATION, INC. AND SUBSIDIARIES; RAYCOM TV BROADCASTING, INC., AS SUCCESSOR-IN-INTEREST OF COSMOS BROADCASTING CORPORATION AND AFFILIATES, PETITIONERS,

v.

JONATHAN MILLER, SECRETARY OF THE FINANCE AND ADMINISTRATION CABINET OF THE COMMONWEALTH OF KENTUCKY; COMMONWEALTH OF KENTUCKY, DEPARTMENT OF REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF KENTUCKY

PETITIONERS' REPLY BRIEF

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The Petitioners, Johnson Controls, Inc., Security Group, Inc. and Subsidiaries, including Sargent & Greenleaf, Inc.; Willis North America, Inc. and Affiliates; Bunzl USA, Inc. and Subsidiaries, including Mak-Pak, Inc.; Tredegar Corporation, Inc. and Subsidiaries; and Raycom TV Broadcasting, Inc., as successor-in-interest of Cosmos Broadcasting Corporation and Affiliates, respectfully submit this Reply Brief in response to the Respondents' Brief in Opposition ("Opposition Brief" or "Op. Br."), and in further support of the Petition for Writ of Certiorari to the Supreme Court of Kentucky ("Petition") in the case of *Jonathan Miller, Secretary of the Finance and Administration Cabinet of the Commonwealth of Kentucky, et al. v. Johnson Controls, Inc., et al.*, 296 S.W.3d 392 (Ky. 2009). The Opinion of the Kentucky Supreme Court is reprinted at Petitioners' Appendix ("Pet. App.") 1-76.

I. INTRODUCTION

A grant of certiorari is appropriate in this case because of the egregious error made by the Kentucky Supreme Court in applying the important judicial precedents of this Court, which resulted in a denial of due process. Equally important, certiorari is appropriate because of the slippery slope onto which the Kentucky opinion, if it is not reviewed, will potentially place taxpayers across the country. Indeed, nothing in the Opposition Brief addresses the far-reaching, adverse consequences of the Kentucky Supreme Court's decision. Initially, rather than

providing the Court with reasons that the Petition should be denied, the Respondents provide an eighteen page "Statement" hardly germane to the merits of the dispute between the parties – much less to the question of certiorari. This "Statement" is followed by nine pages of argument asserting that a state legislature has an unfettered right to invoke sovereign immunity without regard to any limits that might be imposed by the federal constitution. However, this argument has been clearly rejected by each of the three courts in which it has been raised. Finally, the Opposition Brief concludes with eight pages that primarily address the merits of Petitioners' claims.

In reply, the Petitioners will forego a lengthy repudiation of the factual assertions unsupported by the record and other clear errors set forth in the Respondents' "Statement" and, instead, will focus on three salient points: (1) the potential adverse consequences of allowing the Kentucky opinion to stand without further review; (2) the lack of merit of the Respondents' sovereign immunity argument as a reason for denying the Petition; and (3) a showing that the Opposition Brief actually supports the granting of the Petition.

II. THE ADVERSE CONSEQUENCES OF ALLOWING THE KENTUCKY OPINION TO STAND

The national import of this case is demonstrated, in part, by the fact that three major business taxpayer advocacy groups in the country – Council on State Taxation, Institute for Professionals in Taxation and Tax Executives Institute, Inc. – filed *amicus curiae* briefs in support of Petitioners. This is because the approach employed by Kentucky in this case – if followed nationally, will encourage states to address their budget woes by first demanding taxes not due, and by then later escaping the duty to refund the tax overpayments by legislatively eliminating all refund claims filed.

The projected total budget shortfall for the 50 states for 2010-2011 is estimated to be $375 billion.[1] One way of easing these budget deficits would be for each state to adopt the approach employed by the Kentucky Revenue Cabinet and Kentucky General Assembly in this case (as sanctioned by the Kentucky Supreme Court). The approach works like this – the executive branch taxing authority applies an aggressive, overreaching and unlawful interpretation of a taxing statute to increase state revenues. Because most states, if not all, lack a "pre-deprivation

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[1] McNichols, E. and Johnson, N., *Recession Continues to Batter State Budgets; State Responses Could Slow Recovery*, Center on Budget and Policy Priorities, (February 25, 2010), http://www.cbpp.org/cms/?fa=view&id=711.

remedy" many taxpayers will comply with the potentially erroneous statutory interpretation when filing their tax returns. They will do so to avoid the imposition of interest and penalties and a payment of tax will be made in reliance on the "clear and certain remedy" promised by the refund statutes of their respective states, which are required by the Due Process Clause of the Fourteenth Amendment[2] as interpreted by this Court in *McKesson Corp. v. Division of Alcoholic Beverages & Tobacco*, 496 U.S. 18, 32 (1990), *quoting Atchison, T. & S.F.R. Co. v. O'Connor*, 223 U.S. 280, 285 (1912). Then, when the taxpayers learn that the taxing authority's interpretation was erroneous and they file proper refund claims, the legislature acts to retroactively extinguish the claims – thus allowing the state to keep monies to which it was not entitled in the first place.[3] The best

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[2] "Nor shall any State deprive any person of life, liberty, or property, without due process of law." U S. Const. amend XIV, § 1.

[3] This scenario mirrors the facts of this case. Together with passage of statutes with excess retroactivity this scenario is being played out in similar or analogous fact patterns in California, Michigan and Virginia within either the states' administrative process or lower courts The battle continues to rage in Kentucky – *see* the Brief of *Amicus Curiae* Kentucky Chamber of Commerce and *Johnson Controls, Inc , et al. v Commonwealth of Kentucky, Finance and Administration Cabinet, et al.*, U.S. District Court, Eastern District of Kentucky, Central Division at Frankfort, Civil Action No. 3:07-CV-65 Furthermore, the ten year battle that began with *South Central Bell Telephone Co. v. Alabama*, 526 U S. 160 (1999) has only recently concluded. *See Ex parte Vulcan Lands, Inc.*, 6 So. 3d 1157 (Ala. 2008), *on remand at, remanded by Vulcan Lands, Inc.*

(Continued on following page)

reason for granting certiorari in this case is to stop the states from charging down this unconstitutional and confiscatory slippery slope dragging taxpayers with them.

III. SOVEREIGN IMMUNITY IS NOT APPLICABLE TO THIS CASE AND THEREFORE, CANNOT BE A BASIS FOR DENYING THE PETITION

The Respondents assert, "Petitioners' tax overpayment claims are barred by well settled principles of state sovereign immunity which do not need to be rehashed on certiorari." Op. Br. at 19. A portion of the Respondents' statement is true; that is, "well settled principles of state sovereign immunity [ ] do not need to be rehashed on certiorari." This is because the idea that the Petitioners' refund claims are barred by passage of KRS § 141.200(17) has been rejected by every court to which it has been addressed.

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v Surtees, 6 So. 3d 1164 (Ala. Civ. App 2008). *See also Triple-S Management, Corp. v. Municipal Revenue Collection Center*, No KLAN200701749 and No KLAN200800249 slip op. (P.R. July 17, 2008) (unpublished), *request for cert denied* (P.R.S C. March 16, 2009), and *motion for reconsideration denied* (P.R.S.C. April 28, 2009), and *second motion for reconsideration denied* (P.R.S.C. May 27, 2009), *petition for cert. filed*, 78 U.S.L W. 8, p. 3099 (U.S August 25, 2009) (No 09-233) (Puerto Rico Supreme Court upheld administrative action by the Municipal Revenue Collection Center to retroactively impose property taxes for a period of fifteen years).

On this issue, the Franklin Circuit Court (the trial court) held, "The Defendants unconvincingly assert the defense of sovereign immunity." Pet. App. p. 108, fn. 4. The Court of Appeals of Kentucky next held: "Upholding the Cabinet's sovereign immunity claim would, therefore, improperly extinguish appellants' clear right to seek a post-deprivation remedy." *Id.* at 97. Finally, both the majority *and* dissenting opinions of the Kentucky Supreme Court cite this Court's opinion in *Alden v. Maine*, 527 U.S. 706 (1999) as being dispositive of the Respondents' argument. Pet. App. pp. 11, 55-57. In *Alden*, this Court held: "The constitutional privilege of a State to assert its sovereign immunity in its own courts does not confer upon the State a concomitant right to disregard the Constitution or valid federal law. * * * Rather, certain limits are implicit in the constitutional principle of state sovereign immunity." 527 U.S. at 754-755.

Much of the Respondents' lengthy sovereign immunity argument is based on an improper framing of the issue and citations to cases not applicable to this case. Specifically, Respondents improperly frame the issue as whether a state's consent to suit confers a property right protected by due process. Op. Br. at 19-28. However, the proper question is whether the state can eliminate an existing property right arising under the federal constitution (*i.e.*, the right to post-deprivation relief from exaction of unlawful or

erroneous taxes),[4] by simply withdrawing its "consent" to be sued. This question has been addressed by this Court and the answer is "No". As a result, the Petitioners' claims are not barred by sovereign immunity, and the doctrine therefore does not serve as a basis for denying the Petition.

IV. THE OPPOSITION BRIEF SUPPORTS GRANTING THE PETITION

The Respondents assert that the Court should reject the Petition because, "The Court has already provided ample 'guidance' on the 'due process limits of retroactive legislation.'" Op. Br. at 28. Thus, if this assertion is incorrect, this Court should accept review. As shown in the original Petition, and as further addressed below, much remains unsettled after this Court's decision in *U.S. v. Carlton*, 512 U.S. 26 (1994).

A. Unresolved Questions Concerning the Standard Articulated in *Carlton*

As an initial matter, courts have taken conflicting positions on whether due process merely

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[4] The Commonwealth has enacted two applicable refund statutes: a specific income tax refund statute, KRS § 141.235; and a general tax refund statute, KRS § 134.580. By enacting these tax refund statutes, the Commonwealth has provided taxpayers the constitutionally required clear and certain remedy for an overpayment of taxes. *See also Revenue Cabinet v. Gossum*, 887 S.W.2d 329, 333 (Ky. 1994).

requires that states have a "rational basis" for implementing a retroactive tax statute or whether there is a two-part (or three-part) test for determining whether a retroactive tax violates the Due Process Clause (*i.e.*, requiring a rational purpose for the retroactivity *and* a modest period of retroactivity *and* prompt legislation).[5]

As alluded to above, courts are at odds as to whether the second prong of the test from *Carlton* contains its own two-part test requiring both a modest period of retroactivity *and* prompt legislative action, or whether it requires only a modest period of retroactivity. *Compare IEC Arab Ala., Inc. v. City of Arab*, 7 So. 3d 370 (Ala. Civ. App. 2008) (discussing only modesty) *and Baker v. Ariz. Dep't of Revenue*, 105 P.3d 1180, 1186-1188 (Ariz. Ct. App. 2005) (discussing only modesty) *with City of Modesto v. National Med, Inc.*, 128 Cal. App. 4th 518, 528, 529 (2005) (discussing both promptness and modesty). Furthermore, as described, on pages 16-19 of the Petition, there has been much discussion of what constitutes a "modest" period of retroactivity.

With regard to legislative promptness, the Respondents chastise the Petitioners for "asking the

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[5] In this case, the precise test relied upon by Kentucky Supreme Court appears to be something of a hybrid – "retroactive application of a statute need only be (1) supported by a legitimate legislative purpose (2) furthered by rational means, which includes an appropriate modesty requirement." 296 S.W.3d at 399, Pet. App. p 16

Court 'to establish that retroactive legislation violates due process when a state legislature fails to enact the legislation at the first possible legislative session.'"[6] Op. Br. at 28. The respondents continue, "Presumably this Due Process Clause requirement would shackle Congress as well." *Id.* In fact, Congress has set its own limits. In *Carlton,* the Court recognized that the brief retroactive nature of a curative statute is a "customary congressional practice," one that is generally confined to short and limited periods required by the practicalities of producing national legislation. 512 U.S. at 33 (*quoting U.S. v. Darusmont*, 449 U.S. 292, 296-97 (1981)). The variety of opinions in the cases cited above establish, and require, that this Court has the last word on the standard for analyzing a retroactive tax statute. Thus, granting the Petition is proper.

B. Confusion Exists as to the Reach of *McKesson*

The Kentucky Supreme Court took the position that *McKesson* applies only to situations in which the tax statute generating the refund claim is found to be in violation of the constitution. *Johnson Controls*, 296 S.W.3d at 402. Pet. App. pp. 24-25. The Respondents

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[6] In its Opposition Brief, the Respondents make numerous statements in support of the idea that the Kentucky General Assembly acted at the first possible legislative session. Op. Br. at 10-15, 29, fn. 14. The record, if cited in its entirety, does not support such a claim.

set forth this position on pages 25-28 of the Opposition Brief with regard to both *McKesson* and *Reich v. Collins*, 513 U.S. 422 (1998). To reach this conclusion, though, both the Kentucky Supreme Court and the Respondents had to ignore the precedent leading up to *McKesson* and *Reich* and, instead, had to view those two cases in a vacuum. For example, nearly 100 years ago the Court in *Atchison* did not limit the scope of due process remedies to only constitutional violations. The Court held:

> It is reasonable that a man who denies the legality of a tax should have a clear and certain remedy. The rule being established that, apart from special circumstances, he cannot interfere by injunction with the state's collection of its revenues, an action at law to recover back what he has paid is the alternative left. Of course we are speaking of those cases where the state is not put to an action if the citizen refuses to pay. In these latter, he can interpose his objections by way of defense; but when, as is common, the state has a more summary remedy, such as distress, and the party indicates by protest that he is yielding to what he cannot prevent, courts sometimes perhaps have been a little too slow to recognize the implied duress under which payment is made. But even if the state is driven to an action, if at the same time, the citizen is put at a serious disadvantage in the assertion of his legal, in this case of his constitutional, rights, by defense in the suit, justice may require that

> he should be at liberty to avoid those disadvantages by paying promptly and bringing suit on his side.

223 U.S. 280, 285-286. The court below and Respondents simply turn a blind eye to the roots of the holdings in *McKesson* and *Reich* – roots implicit in the expansive language used by the Court in *McKesson* requiring a clear and certain remedy "for *any erroneous or unlawful tax collection* to ensure that the opportunity to contest the tax is a meaningful one." 496 U.S. at 39 (emphasis added).

Furthermore, taking the Kentucky Court's and Respondents' position to its logical conclusion would mean that *McKesson* and *Reich* have no precedential value other than to factual situations identical to those cases. The narrowing of the due process rights of taxpayers by the Kentucky Supreme Court, and as urged by the Respondents, is reason enough that this Court should grant the Petition.

C. Respondents' Mischaracterization of the Petitioners' Equal Protection Argument Is Not a Reason to Deny the Petition

On pages 32-35 of the Opposition Brief, the Respondents conclude by first reintroducing their sovereign immunity argument and then by describing the different treatment of "'similarly situated taxpayers'" as a "function of the effective date of the two statutes [KRS § 141.200(17) and KRS § 141.200(18)], not of any legislative classification among taxpayers."

Op. Br. at 33. The Petitioners' equal protection argument is set forth at pages 19-24 of their brief and will not be repeated here. Suffice it to say that Petitioners' equal protection claim is not based on the date of two statutes; rather it is based on similarly situated taxpayers being treated differently prior to the date selected by the statute (December 22, 1994). Thus, the 2000 Amendments, as applied, worked an unconstitutional discrimination against the twenty-nine taxpayers at whom those amendments were directed. This discrimination warrants granting the Petition.

V. CONCLUSION

For the reasons set forth in their Petition for Writ of Certiorari and herein, the Petitioners respectfully request that the Petition be granted.

Respectfully submitted,

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